MDM Bank & URSA Bank Joint Conference Call
9th December 2008
Chaired by Vadim Sorokin and John McNaughton

Vadim Sorokin

Good afternoon, ladies and gentlemen. Actually, before we start the actual conference call I would like to state one thing; that today we have a call not from MDM side just but from side of two banks, which is MDM and URSA bank and actually that's the topic we are going to cover today because the overall idea for you to listen about the recently announced merger between these two institutions. Two words about the history of the overall transaction and the idea behind it: Our shareholders have been discussing this transaction over the last several months, and during the last month they finally came to the agreement to announce that transaction was announced recently December 1st.

How they see the transaction. What they take is they take the crisis situation not from any downside: they take the crisis situation as a potential opportunity and they really believe that the overall idea to measure institutions, is to bring together two institutions, which have their strengths and weaknesses of course, and to bring this under one umbrella first and will go about their transaction structure in a second. And finally to merge two institutions as one leading, strong private bank in Russia.

This transaction goes in line with the overall idea of the Central Bank of Russia and the government of the Russian Federation with respect to consolidation of Russian banking system. And by this consolidation actually they mean and we mean not consolidation of all weak institutions under the strong institutions but rather consolidation of strong institutions to become even stronger.

In terms of our two organisations, we believe that we will have very good geographical product and business combination. On URSA side, for example, there is a very strong franchise on the retail business. On MDM side, we get very strong franchise on the corporate business, so a combination of these two businesses will bring our institution to absolutely different level from where we are now. With respect to, for example, geographical coverage, we are at MDM are presented quite good in a central part of Russian Federation; URSA is presented quite good on a Siberian and eastern parts of Russia.

The overall idea between our shareholders was to make a friendly transaction with the mutual interest and they bring their shares in the holding company, which will be managed together by them on an equal basis. We have a lot of synergies with respect to this transaction and during the presentation we will try to cover it. Of course if you will have any questions at the end we'll be happy to answer those. With respect to the funding, we will have much stronger position on both corporate side and retail side and as soon as capital markets will open, we believe we'll have much better proposition to the market than we have now. Next slide, please.

The overall structure of the transaction: So far it is planned to be done through three stages. With respect to stage number one, there will be a holding company under which there will be two banks working in parallel for some time and all shareholders of MDM and URSA will have their shares in this holding company. On stage two, two banks will go into the legal merger and stage three is basically a merger of the holding company into the merged bank. Right now there are discussions – as I said, that's the preliminary structure – right now there are discussions to bring stage two and stage three together so it will be finalised on the later stage. Next slide, please.

On this slide you can see the legal structure of the transaction: on top there is a holding company for which we will use MDM holding company, which exists now, and underneath there are two banks: MDM Bank and URSA Bank. In terms of the stage one of the transaction it is planned that preferred shares and preferred shareholders will not participate in stage one so all preferred shares will stay in both banks and will not go to the holding company and during stage two and stage three, preferred shares will go in line with all other ordinary share holders. Next slide, please.

When the overall transaction was planned, we allocated a sufficient amount of time to every stage. That would allow us to make sure that we undertake all necessary legal and operational steps we have to, and receive all approvals we need to receive to comply with all legislation. Also we have taken into account any potential tax issues. The overall analysis, which we've done with respect to tax gives us the comfort that in most cases, there will be no tax liabilities, and if there will be, they will be very minimum.

The commercial factor for a change of shares between shareholders of two banks will be defined using the method of adjusted net assets value. The methodology for this calculation has been agreed. Their final calculation will be done based on IFRS numbers as of December 31st 2008. As I mentioned already, Mr Popov and Mr Kim will generally maintain controlling stake in the merger bank and preferred shareholders will be converted into the preference shares of the merged bank, stage two. Next slide, please.

Before we had announced the transaction on December 3rd, all existing shareholders have signed a memorandum of understanding. So that covers the overall concerns of all existing shareholders and their support for the transaction.

We have started our discussions with some of our shareholders in terms of additional subordinated debt to be raised for the merged bank so these conversations are under way. We have received commitment to maintain the shareholding from all shareholders with a horizon of at least five years. And also we have right now negotiations with international financial institutions in terms of additional funding of the merged bank.

Before the transaction was announced, we have had numerous discussions with regulators and the government of the Russian Federation, and on each level actually we talked to, we received 100% support for this transaction. And as I have mentioned already, this transaction goes in line with the overall strategy of the Central Bank with respect to the consolidation of the banking system and based on that, there was great support from all authorities for that transaction. Next slide, please.

On this slide you can see the shareholding structure of both banks, MDM Bank and URSA Bank. The total structure, which includes preferred shares, and the voting structure, which excludes preferred shares on URSA side but includes preferred shares on MDM side given the fact that MDM bank does not pay dividends to their preferred shareholders and therefore they are voting shares. Next slide, please.

As one of our fundamentals for this transaction there was an agreement achieved between all shareholders that the merged bank will maintain their high standards of corporate governance in this country, and for that there will be created the new board. This board will have all necessary committees and the composition of this board will support their idea of high standards of corporate governance.

We have received pre-approvals from all authorities going forward. Before we go into even the first stage, we will receive necessary approvals from the Central Bank of the Russian Federation, Federal Antimonopoly Services, and Federal services on financial markets, if necessary. Also within our plans on stage one is to handle negotiations with all creditors with respect to covenants we have with these creditors. Until the timeline, it is planned to complete stage one by July 1st 2009. Legal merger to banks to complete by the yearend 2009 and to perform integration within the next 12-18 months, subject to any developments which will happen during that time. Next slide, please.

We appreciate that there is an execution risk for this transaction and before we have entered into it, there was a plan designed to mitigate this risk. As a few of our mitigation factors, we can mention that this is a merger of two equals based on a friendly desire of all shareholders. We have received support from the Central Bank and other operators. As the new CEO of MDM bank and the Joint Bank, Mr Kim will be appointed, and his MMA track record, as he has done six similar transactions, will be one of these mitigating factors to eliminate execution risk.

As I have mentioned we do not have that many business overlaps, therefore this risk, we believe, is minimal. We do not need any either usual or unusual additional debt or equity financing for that transaction, therefore it’s not an issue given the current market situation. On some of the next slides you will see the graph, which shows the liquidity position of individual banks and of the merged bank. From that graph you will see that we have significant liquidity cushion so we have covered that risk as well. And given that we are doing the national merger and we are strong institutions in our home market, we believe that will help in the transaction as well. Next slide, please. I will hand over to John.

John McNaughton

All right. Thank you. First of all, thank you, everyone, for joining the call. Statistics show that we have over a hundred people so I see that the interest on this merger is quite great. Indeed it is a great merger that we’re speaking about and I thank you, Vadim for talking about the, taking the first part of the presentation, which was the more difficult one so I get to speak about the easy part of the presentation: this is about the strategic rationale.

The fact that MDM and URSA bank are merging is very clear when you look at the two banks as separate entities, URSA bank again being the strong regional bank, MDM bank being the strong centrally based bank. When you look at each bank individually and add them up, the combination of the two is much stronger than the sum of its parts.

If you look at the business that we will be having as a joint bank, URSA bank gets coverage into the corporate sector whereas MDM gets more coverage onto the retail side. The enhanced creditworthiness that we have in terms of the customer base will be strengthened considerably.

We are both privately owned banks, and after the merger we will become if not the largest, one of the two largest privately owned financial institutions in the country. With such a strong financial institution we'll have sufficient scale, not only to ensure stability for its clients but also to be a major financial powerhouse in this country.

For those that know MDM and URSA bank, MDM has always been rated number one among all Russian banks for the level of corporate governance. URSA bank has also high standards. On the Standard and Poor's list we were rated number four last year but still with the combination of international financial institutions on the board of directors and as shareholders we have been pushing both our two banks to the highest levels of corporate governance. The merged bank will continue to adhere to these standards. And again when you're merging two banks such as ourselves, the business synergies and diversification of the asset pools are tremendously increased, again more than the sum of its parts.

The other strategic rationale has to do with the current environment and as we've said, this is a merger of equals, two strong banks. The timing of this merger is a matter of fact happening in today's current crisis, not because of the crisis situation but it gives us an opportunity to see the business opportunities that are emerging in today's environment. A lot of the weaker banks are dropping out, which will give us as a merged bank, again the largest privately owned bank, a much greater opportunity to continue to serve the banking customer set here in Russia.

Next slide: slide 11. Looking more concretely into the aspects behind the strategic rationale, as I mentioned, creating one of the largest privately owned banks in Russia, we will be a top ten player in a lot of the markets. If URSA bank was already a top player in Siberia, the Urals, in the Far East, MDM is a top player in Moscow and the European sectors of Russia. Now we will be a top player in all of the markets pretty much.

Again the cultures and the business models of the bank are somewhat similar. Again, as privately owned banks adhering to high levels of corporate governance, the management of the two banks is like-minded in its goals and its culture. And imagining the regional presence again, the strengths are so apparent in the fact that our geographic footprints have not crossed in any major degree.

And on the cost savings, why do banks merge? Not only to become stronger but to work at cost savings across the board. Although there's little overlap, we will definitely have certain areas where we'll be seeing cost savings throughout the years. The obvious ones are the integration of an IT platform, the redundancy of structures that would be able to be eliminated and the centralisation of the operating centres of the bank.

Now page 12 please: the next slide. Speaking about better access to funding, of course in today's environment, most banks are focussing on increasing the retail and corporate deposits in its home market. The greater size and the stability of the merged bank will definitely be able to give us better access to both of these pools of funding, more access to corporate clients, larger limits because obviously the joint equity of the bank will now be increased, a larger branch network. You'll see that while both of us had in the range of over 200 branches, the combined bank will have over 400 branches, and more increase to government funding. The central bank funding ministry of finance and other government owned organisations that are continuing to create deposits in Russian banks will be increased.

The wholesale debt funding, currently the markets are closed. However as soon as they start to open, I think the merged bank will definitely have a much better access to these markets than other non-state owned banks here in Russia as well as having increased limits by foreign and local investors.

If you look at the next slide, slide 13, you can see how we would jump up the charts in terms of our rankings here in Russia. If you look at the joint assets of the banks and the joint equity of the banks you will see that where we ranked in the teens, both MDM and URSA bank, we will now be ranked up within the top ten banks of Russia. This is very important. In both speaking with our clientele and speaking with foreign and local investors, size really does make a difference in our markets.

Page 14, next slide, will show you how we rank in terms of market share. People familiar with the banking sector here in Russia know that the banking sector is dominated by the top five state owned banks and in addition to those banks, there's another over 1,000 banks in the market.

As individual banks, URSA bank, even though we're the largest bank in Siberia and MDM bank also being a very large bank, can only command less than 2% of market share in this country. Combine the banks with an increase in presence and an increase in power and support, we expect we can increase the market share across the corporate lending, retail lending, retail and corporate deposits to over 4%.

If you look at the next slide, page 15, shows you the map of where branch networks will be located throughout the country. You can see from the chart that the 240 branches of URSA bank and the 205 of MDM will create the third largest network of non-state owned banks here in Russia. We do obviously have some overlapping cities, especially in the Urals and Siberia where we would make an individual decision based on the businesses of both branches of what to do. We might keep them both or combine the branches for additional cost savings.

If you look at page 16, next slide, we'll see basically an overview of the fundamental financial figures of MDM, URSA and what a merged bank would look like. Over 450 branches, 12,000 corporate SME customers, an additional 35,000 small and medium business customers, over 2 million retail customers with over 2.5 million plastic cards issued, over 1,300 ATMs. This will really put is in the top league among all of those indicators.

Page 17, the next slide: One of the most important slides or figures to show you in today's environment. Both URSA and MDM bank have always followed conservative liquidity management procedures. In addition to conservative underwriting procedures, especially starting in 2007, both URSA and MDM bank now have a joint liquidity cushion of over 70 billion roubles. This represents a large percentage of the overall assets of both banks in liquid assets.

We also have, as you can see in the graph, the chart going up to the end of 2009. We expect this large liquidity cushion to serve us well in the current environment.

Page 18, next slide: Just a conclusion of the overall merger slides. Creating Russia's second largest privately owned bank with the universal banking franchise to become a top player in the retail and corporate banking products and markets, to have a national network coverage of over 150 cities in the country, serving over 2 million retail and 47,000 corporate and SME clients, offering an expanded range of financial services, both in corporate and investment banking and retail banking as well and more diversified business and income structure and again from numerous synergies, arising from cost efficiencies, rationalisations and complementary business model and enhanced business network. And of course a bigger reliance on the stable and diversified base of shareholders with a long-term strategy.

If you go and look at the next slide, page 19, I won't go into this in detail. Both MDM and URSA bank have robust websites. You can download all of our latest information whether on MDM or URSA bank's site. Obviously if you have any questions, we're always available at the emails that you can find in the website and I guess we're also available right now to answer your questions. This is the end of the official part of the slide presentation but we'll be here and awaiting your questions. Thank you very much.

Questions and Answers

Kay Turner – Citi Group, London

Three questions if I may. The first one was has the government provided any financial or otherwise support in terms of helping this transaction to go through? Secondly, could you confirm, I'm not sure that I actually heard where the key shareholders' stakes will be on the combined entity. And I was just wondering if you could confirm whether those stakes in the entity will ensure that there's no change of control in any of the outstanding obligation?

John McNaughton

Yes, let me just address that question. On the first stage, on the government support, obviously before embarking on such a merger, we will be the largest merger ever in Russian banking history, the shareholders and management went out to get the government support, and not only the Central Bank and the Federal Monopoly Service but also the government itself, has voiced their support for this transaction.

In terms of actual funding support, this obviously remains to be seen and there have been no guarantees been received from the federal government they will provide funding support. Obviously with the liquidity that we have currently, we're not in need of any funding support and with the capital ratios that we have currently also we're overly capitalised.

However, Vneshekonombank does have the lines that have been pre-approved both for the subordinated debt, to fund the subordinate debt of each bank as well as some other programmes that the Russian Development bank is working on in terms of SME on lending facilities and other types of programmes that despite having a merger, would still have been in place had we gone forward or not. And these in general have been orally confirmed to be continued without any changes.

In terms of your second question, if you look at slide seven, you will see the current situation in terms of the shareholders of the banks. We did not put the joint shareholding on purpose because this joint shareholding at the end of the day after the merger has been completed, has not been resolved and maybe missed this point. It will be based on the yearend IFRS account and so until those are ready, the percentage of shareholders in the new merged entity will not be known. Hopefully that will be made clear in the first or second quarters of next year.

And your other point regarding the change of control governance: obviously this is something that we are going to be working on. Obviously a change in control will trigger a certain change of control covenants in certain agreements. This is again one of the risks associated with the mergers. We have hired legal counsel to advise us on this but we don't expect that this will be a major hindrance in the course of this merger.

Vadim Sorokin

Just a couple of words. Today with respect to the government support. Today there was a meeting between our chairman of the board of directors so far, MDM Mr Viyugin who will be actually the chairman of the board of directors of the merged bank and the prime minister of the Russian Federation, Mr Putin and during that meeting there was strong support mentioned by Mr Putin for that transaction.

Fantastic. Could I just ask one last question before I turn it over to others? In your perception – this is obviously not regarding the transaction but it's more specific to Russian banking – is the population more or less sensitive to a slow devaluation or a hard devaluation and how do they react in terms of deposits?

I'll start and John will continue I assume. Of course we need to put in front certain disclaimers for this answers so you won't use it for any purpose. Of course I think the population is sensitive to any changes of the exchange rate of Russian rouble because over the last several years, the population tends to convert all foreign currency saved into Russian roubles although over the last I think few months what we notice is a serious transfer from Russia roubles into hard currency – primarily US dollars. Those are, we believe that given the, if rather Russian rouble will further devalue, I think this trend will continue on the one hand. On the other hand, on our side we didn't notice significant outflow of individual deposits. Actually over the last month of November, we saw inflows of individual deposits of 7%.

John McNaughton

Yes, I'll just add to that. You have two things going here. First of all is that the fear of a rouble devaluation but again that has, and there was an outflow in October pretty much systemised at URSA bank also. This has stopped. November and December have seen an inflow of retail deposits.

The other thing is that of course the central bank raising refinancing rates so the rates that the banks are offering on rouble deposits have been going up and this is also been able to have an effect this inflow of retail deposits as well as the increase in the amount that's secured by the deposit insurance fund here in Russia. So the government is taking the right steps I think to cushion any rouble devaluation that might occur in the future.

Just on the hard or the soft devaluation and the expected reaction by the population as a result of that?

It's difficult to tell. There have been lots of hard devaluations in the past. You know, once a devaluation happens, usually that hits the bottom and then the people that haven't gotten out in time see the rouble then starting to go up so you have that effect and then there's soft devaluation hasn't happened and it's very difficult to give some sort of historical precedence to but you did see again, being softly devalued and over the last two months it showed that there was a peak of concern within two weeks in October and that peak has died out.

Thank you very much for the colour.

Alex Williamson, Finisterre Capital London

Two quick questions: First of all in the presentation you mentioned potential subordinated debt support from existing shareholders. Would that be into the newly formed Holdco or would that be split between the two individual banks underneath the Holdco?

At this stage it would be underneath the Holdco [*the Holding Company*] because the two banks have existing banking licences and in order to get matching subordinate debt from Vneshekonombank, it would have to be to an existing banking companies with licenses but of course those will be merged.

Do you have any concept of what the split would be and what the quantums involved are?

Do you mean the split between the two banks?

Yes.

Well, in general, Vneshekonombank is reporting 15% and that might be raised but as of now 15% of equity, which is roughly, at URSA bank that would translate into 150 million matching subordinated debt from Vneshekonombank bank to another 150 million from shareholders resulting in a maximum 300 million. From MDM…

Vadim Sorokin

From MDM side 15% would equal roughly 6 billion roubles, which should be matched by the same amount from the existing shareholders and again if this money will be needed, we can get those.

Okay, last question: This one is what's the contemplated timing of those actions?

There are three stages: Stage one we approximately estimate about six months.

Sorry, I meant the contemplated timing of the subordinated capital injections.

Well, for URSA bank we're expecting to receive the first $100-150 million in the first quarter and the matching 150 million or 100 whatever it happens to be within a month after the first stretch, so that might get into the second quarter.

Vadim Sorokin

Actually for MDM we do not have recent plans to use this facility but as I mentioned if it will be needed, we will use it.

Thanks. And my second question is what is the contemplated structure for combining with the two banks' preference shares? You mentioned that…

Well, in terms of URSA bank, because we have listed preference shares, if you look, you can look at maybe slide four, you'll see that at URSA bank, preference shares make up a large amount of capital, about 20% so this is quite relevant. The preference shares will stay at URSA bank while the voting shares will be transferred to the bank holding company. Then finally the two banks will be merged and the preference shares will then remain with the merged entity and would not have to be transferred from the bank holding company because they will already be existing with the merged entity.

Vadim Sorokin

In terms of preference shares for MDM, it's very simple because as I mentioned already, these shares are ordinary shares and the fact they are ordinary shares, therefore we don't expect any differences for existing shareholders given that this preference shares are owned by exactly the same shareholders from the ordinary side.

Great. Thank you.

Svetlana Kovalskaya, Renaissance Capital, Moscow.

Hello Vadim and John and thanks very much for holding this conference call today. My question is also on preference shares. Could you please just go through it again in terms of how the actual economics terms of these transactions for the preference shareholders will work out?   I mean there will be certain conversion qualifications for the common shares from the, say URSA bank, into the merged entity and then will the same qualification be applied to preference shares and just generally how is it going to be?

John McNaughton

Well, the general idea that URSA bank preference shares will not lose any of its economic value for its preference shareholders, i.e. all the right and all of the governance issues and all of the issues with the dividend payments will remain the same when they get transferred into the merged bank. Now as for the valuation, yes, they will be treated the same valuation as the ordinary shares and this again will be determined… It will actually be determined and approved by independent bodies within the first or second quarters of next year.

Okay, thanks.

Sure.

Anna Vlasenkova – BNP PARIBAS, Paris

What will be the name of the new bank, please?

Well, so far the name for the new bank has not been yet developed. The old idea to start with the master bank will be either MDM URSA bank or URSA MDM bank and the overall conclusion will be based on the feedback, which we'll receive from our customers later.

Thank you. And just a question about when do you expect the first consolidated financials to appear for the merged bank, please?

Well, given the timeline I outlined I think the first consolidated financial statements, we expect to have at the yearend 2009. If the consolidation will not be completed by that time, it could be any quarter in 2010.

Okay. Thank you.

Slava Zhabin – Troika Dialog Asset

Could you confirm please your decision about preference shares? Is it right that the dividends for the shares will be maintained during this consolidation?

John McNaughton

Yes, that's right. In terms of the articles under the preference shares, there's a minimum dividend payment of 8.1 percent per share or whatever's paid on common dividends if it's a higher amount. This is will remain share right in the merged bank.

Is it right the preference shares will stay on the market after consolidation of the banks?

That's right. We intend to keep the preference shares listed at both the RTS exchange and the MMBB exchange.

The preference shares?

The preference shares.

Only URSA bank preference shares?

Only the URSA bank preference shares. That's correct.

Vadim Sorokin

The preference shares on MDB side are not marketable shares and effectively they are very close to ordinary shares. We don't pay dividends on them and therefore they're voting and belong to the same shareholders as they own ordinary shares.

Thank you.

Closing Comments

From URSA bank side, thank you very much for calling in and we're always available to answer your questions as you may have them.

Thank you everyone for participation and if you have further questions, please don't hesitate to get in touch with us. Goodbye.